BEFORE THE

Federal Communications Commission

WASHINGTON, D.C.

In the Matter of	)	
	)	
Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers	)	CC Docket 95-185
	)	
Equal Access and Interconnection Obligations Pertaining to Commercial Mobile Radio Service Providers	)	CC Docket 94-54

COMMENTS OF THE
CELLULAR TELECOMMUNICATIONS INDUSTRY ASSOCIATION

Michael F. Altschul
Vice President, General Counsel

Randall S. Coleman
Vice President for
Regulatory Policy and Law

CELLULAR TELECOMMUNICATIONS INDUSTRY ASSOCIATION
1250 Connecticut Avenue, N.W.
Suite 200
Washington, D.C. 20036
(202) 785-0081

Philip L. Verveer
Jennifer A. Donaldson
Michael G. Jones
Thomas Jones
WILLKIE FARR & GALLAGHER
1155 21st Street, N.W., Suite 600
Three Lafayette Centre
Washington, D.C. 20036-3384
(202) 328-8000

Of Counsel

March 4, 1996

SUMMARY

CTIA supports the Notice's tentative conclusions and urges the Commission to adopt expeditiously a comprehensive reciprocal termination plan, i.e., bill and keep, to govern interconnection compensation between LECs and CMRS providers. The Commission's proposals to quickly adopt reciprocal termination to govern the interconnection compensation relationship between CMRS providers and the LECs are sound. They will foster the competitive development of the CMRS market and afford significant competitive opportunities for the local exchange. Specifically, CTIA proposes the following:

- As a matter of policy, the Commission should adopt a reciprocal termination requirement.
- By adopting reciprocal termination, the Commission need not impose tariffing and other costly, ongoing reporting requirements on the LECs.
- The Commission has the requisite authority, if not the obligation, to adopt a comprehensive reciprocal termination requirement, and to preempt any contrary state regulation.
- The Commission should defer consideration of CMRS provider eligibility to receive access charge payments to the access charge reform proceeding.
- Consistent with the principles of regulatory parity, the Commission should require reciprocal termination to govern interconnection arrangements among all CMRS providers vis-a-vis the LECs.

TABLE OF CONTENTS

I. INTRODUCTION 2

II. AS A MATTER OF POLICY, THE COMMISSION SHOULD ADOPT A RECIPROCAL TERMINATION REQUIREMENT. 7

A. Reciprocal Termination Will Properly Account for the Disparity in Market Power Between the LECs and Their CMRS Competitors. 9

B. Reciprocal Termination Sufficiently Approximates Carrier Marginal Costs for Traffic Termination. . . 20

1. Reciprocal Termination Will Allow Carriers to Recover the Cost of Terminating Traffic. . . . 21

2. Reciprocal Termination Compares Favorably With Recovering Termination Costs Using Usage Sensitive Rates. 24

a. Neither Reciprocal Termination Nor Usage Based Rates Should Be Preferred Solely on the Basis That Resulting Price Signals Are More Efficient. 25

b. Reciprocal Termination Avoids Efficiency Distortions Associated With Inaccurate Rate Levels. 29

c. The Cost of Implementing Revenue-Based Compensation Arrangements Likely Exceeds Any Possible Benefit. 30

d. Revenue-Based Compensation Arrangements May Result in Dynamic Efficiency Losses by Inhibiting the Development of Competition and Innovation. 31

C. Reciprocal Termination Obviates the Need for Arbitrary and Contentious Cost Allocation Procedures. 34

D. Reciprocal Termination is Appropriate Regardless of the Physical Point of Interconnection with the LEC Network. 43

E. Many of the Major Policy Aspects of the 1996 Act, Including Those Underlying the Interconnection Provisions, Reflect a General Preference for a Reciprocal Termination Approach. 46

III. ADOPTING RECIPROCAL TERMINATION ELIMINATES THE NEED FOR TARIFFING AND OTHER COSTLY, ONGOING REPORTING REQUIREMENTS ON THE LECS. 51

IV. THE COMMISSION HAS THE REQUISITE AUTHORITY, IF NOT THE OBLIGATION, TO ADOPT A COMPREHENSIVE RECIPROCAL TERMINATION REQUIREMENT, AND TO PREEMPT ANY CONTRARY STATE REGULATION. 56

A. Section 332 Provides the Jurisdictional Basis for Commission Consideration of LEC-CMRS Interconnection Compensation, not the 1996 Act's Interconnection Provisions. 58

B. The Commission Has Authority Under Section 332 to Adopt a Comprehensive Reciprocal Termination Compensation Arrangement. 64

C. The Commission Also Has Authority Under Section 2(b) to Adopt a Comprehensive Reciprocal Termination Arrangement to Ensure the Efficient, Competitive Buildout of Nationwide Wireless Communications Infrastructure. 77

V. THE COMMISSION SHOULD DEFER CONSIDERATION OF CMRS PROVIDER ELIGIBILITY TO RECEIVE ACCESS CHARGE PAYMENTS TO THE ACCESS CHARGE REFORM PROCEEDING. 83

VI. CONSISTENT WITH THE PRINCIPLES OF REGULATORY PARITY, THE COMMISSION SHOULD REQUIRE RECIPROCAL TERMINATION TO GOVERN INTERCONNECTION ARRANGEMENTS AMONG ALL CMRS PROVIDERS VIS-A-VIS THE LECS. 85

VII. CONCLUSION 89

BEFORE THE

Federal Communications Commission

WASHINGTON, D.C.

In the Matter of	)	
	)	
Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers	)	CC Docket 95-185
	)	
Equal Access and Interconnection Obligations Pertaining to Commercial Mobile Radio Service Providers	)	CC Docket 94-54

COMMENTS OF THE
CELLULAR TELECOMMUNICATIONS INDUSTRY ASSOCIATION

The Cellular Telecommunications Industry Association ("CTIA"), hereby submits its Comments in the above-captioned proceeding.[1]

In short, CTIA supports the Notice's tentative conclusions and urges the Commission to adopt expeditiously a comprehensive reciprocal termination plan, i.e., bill and keep, to govern interconnection compensation between LECs and CMRS providers.

---

[1] Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers; Equal Access and Interconnection Obligations Pertaining to Commercial Mobile Radio Service Providers, Notice of Proposed Rulemaking in CC Dockets 95-185 and 94-54, FCC 95-505 (released January 11, 1996) ("Notice").

I. INTRODUCTION

To foster the full development of CMRS services as Congress intended, the Commission must strive to adopt policies that produce competition, efficiency, and progressiveness.[2] As the Commission recognizes:

> commercial mobile radio service interconnection with the public switched network will be an essential component in the successful establishment and growth of CMRS offerings. From the perspective of customers, the ubiquity of such interconnection arrangements will help facilitate the universal deployment of diverse commercial mobile radio services.[3]

The rate established to compensate for the exchange and termination of traffic between the LEC and the CMRS carrier is

---

[2] See Regulatory Treatment of Mobile Services, Third Report and Order in GN Docket 93-252, PR Docket 93-144, PR Docket 89-553 9 FCC Rcd 7988, 8010 (1994) (". . . the best way to ensure that we create an enduring regulatory system that applies comparable technical and operational rules to similar CMRS licensees, is to anticipate the potential for increasing competition by providing sufficient flexibility to licensees in our rules. This flexibility will enable them to adapt their services to meet customer demands. If the Commission were to ignore the accelerating pace of technology or the ability of CMRS providers to respond to growing and changing consumer demand for mobile radio services, our technical and operational rules might inhibit rather than promote competition and growth in the mobile services marketplace."); 8017 ("Growth and competition are the defining features of the wireless marketplace. Technology, regulatory policies, and explosive growth in consumer demand continue to propel the expansion of services in the wireless industry. This growth is in part a product of emerging competition in the industry. It will lead to even more competition as various commercial service providers pursue strategies to capture new customers.")(citations omitted) ("CMRS Third Report").

[3] Regulatory Treatment of Mobile Services, Second Report and Order in GN Docket 93-252, 9 FCC Rcd 1411, 1499 (1994) ("CMRS Second Report").

especially crucial to the further development of competition, whether within the local loop or in the national wireless marketplace.

The full realization of the potential of CMRS, however, depends upon the FCC's determined effort to adopt its reciprocal termination proposals quickly. The possibilities for a workably competitive local exchange market also would be advanced substantially by early implementation of the reciprocal termination proposals.

The Notice proposes a sound and practical method of ensuring the continuing development of CMRS and encouraging the competitive development of local exchange services. By requiring that LECs and CMRS carriers[4] terminate each others' traffic free of any accompanying surcharge as the Notice proposes, the Commission would ensure efficient, equitable, and administratively-simple interconnection arrangements.[5] Moreover, it would obviate the need to impose burdensome and costly tariffing requirements on LECs. It also would inhibit the LECs

---

[4] CTIA favors adoption of a reciprocal termination arrangement applicable to all CMRS-LEC relationships.

[5] Reciprocal termination also is consistent with the Commission's regulatory treatment of mobile services generally. See CMRS Second Report, 9 FCC Rcd at 1420 ("Success in the marketplace thus should be driven by technological innovation, service quality, competition-based pricing decisions, and responsiveness to consumer needs -- and not by strategies in the regulatory arena."); 1421 ("one of our objectives in this proceeding is the creation of a regulatory framework that makes access to the wireless infrastructure available to all Americans, at economically efficient prices").

from exercising their still-substantial market power to extract monopoly profits or to hamper the competitive development of mobile services.

Concern over the costs of terminating traffic originating on another network arises only where there is reason to believe that there will be systematic and persistent imbalance in cost and in the quantity of traffic exchanged. There is an imbalance in the case of some types of CMRS traffic, but whether it will persist is much less clear. The CMRS marketplace is being affected by substantial increases in suppliers, by major advances in technology, and by changes in important regulatory requirements, as the Notice evidences. These developments are likely to influence the availability and price of services and the manner in which consumers use them. The dynamic quality of the CMRS marketplace means, among other things, that traffic flows between CMRS and LEC networks could change materially within a relatively short time.

While there are costs associated with traffic termination, the Notice correctly recognizes that these costs are low. In fact, as the Notice recites, many believe that the administrative and recordkeeping costs incurred to track and bill for them may outweigh the underlying costs themselves.

Moreover, any effort on the part of regulators to conclusively allocate these costs is, as a practical matter, futile. As the Notice recognizes, any costing methodology

inevitably will produce arbitrary results because the results are strongly influenced by unavoidable assumptions. Given the dynamism of the market and the complexity of the existing costing methodologies, even if regulators were able to identify and quantify all of the relevant costs associated with LEC to CMRS interconnection compensation, this "correct" result would be obsolete almost immediately. For these same reasons, the Commission should also permit reciprocal termination to control regardless of the physical point of interconnection between the LEC and the CMRS provider.

Rather than expending time and energy on assessing the apparently trivial underlying costs, the Commission should act quickly to adopt its reciprocal termination proposal. The Commission can revisit its decision to adopt reciprocal termination after the CMRS market has matured to correct for any possible resulting market irregularities.

The Commission traditionally has recognized that cellular carriers are co-carriers entitled to mutual compensation for the use of their network facilities to originate and terminate interstate traffic exchanged with local exchange carriers.[6] By taking additional limited action with respect to compensation issues as proposed by the Notice, the Commission will secure an

---

[6] See, e.g., The Need to Promote Competition and Efficient Use of Spectrum for Radio Common Carrier Services, Declaratory Ruling, Report No. CL-379, 2 FCC Rcd 2910, 2915-2916 (1987) ("Interconnection Declaratory Ruling").

efficient result favorable to competition and obviate the most serious potential disputes emanating from unequal LEC bargaining power without substantial interference with the LEC to CMRS interconnection process as a whole.

As a matter of law, the Commission has authority under Sections 332 and 2(b) of the Communications Act of 1934, as amended ("Act"),[7] to adopt such a regulatory regime. Therefore, it can and should preempt in full contrary state regulation in this area to ensure the full maturation and development of CMRS. Moreover, nothing within the Telecommunications Act of 1996 ("1996 Act") undermines the Commission's authority here to adopt a comprehensive reciprocal termination arrangement. In fact, the policy preferences underlying the 1996 Act counsel toward adoption of a reciprocal termination solution generally.

Finally, while CMRS carrier eligibility to receive access charge payments from interexchange carriers ("IXCs") is an important issue deserving the Commission's attention, the Commission would be well-advised to defer consideration of this issue to the access charge reform proceeding.

---

[7] 47 U.S.C. §§ 332, 152(b).

II. AS A MATTER OF POLICY, THE COMMISSION SHOULD ADOPT A RECIPROCAL TERMINATION REQUIREMENT.

The Notice requests comment on a variety of pricing and cost issues associated with adopting a satisfactory short- and long-term pricing structure to govern mutual traffic termination.[8] In this regard, CTIA submits an analysis from Dr. Bridger Mitchell and Dr. Steven Brenner, of Charles River Associates Inc., which examines in detail the economic issues underlying the choice of compensation arrangements to govern LEC to CMRS interconnection compensation.[9] As is demonstrated below, from an efficiency perspective, and as a means to recover the underlying costs, reciprocal termination[10] is more advantageous than traditional means of cost recovery.

The ideal interconnection compensation model for mobile services should promote competition, efficiency, and progressiveness. To do so, it must have the following characteristics:

- account for the disparity in LEC and CMRS bargaining power and for the fact that the interconnecting firms are also competitors;

---

[8] Notice at ¶¶ 26-81.

[9] Dr. Bridger Mitchell and Dr. Steven Brenner, Charles River Associates, Economic Issues in the Choice of Compensation Arrangements for Interconnection Between CMRS and Local Exchange Carriers, (March 4, 1996), attached as an exhibit, (hereinafter "Economic Issues").

[10] CTIA prefers to describe the "bill and keep" pricing structure as "reciprocal termination." Reciprocal termination can be thought of as another form of mutual compensation, where the compensation rate is set at $0.00.

- approximate the underlying costs of providing interconnected service;
- be sufficiently flexible to allow the efficient development of landline and wireless network services; and
- impose minimal administrative costs.

As demonstrated by the following analysis, reciprocal termination is an efficient form of interconnection compensation between LECs and CMRS providers for numerous reasons: it counters the LECs' bargaining power and accounts for the fact that the subject firms are market competitors by removing one of the most controversial issues from the negotiation process; it sufficiently approximates the underlying costs of providing termination services; it is sufficiently flexible to allow the efficient development of landline and wireless network services because its scope is limited to price issues only; and it virtually eliminates administrative and recordkeeping requirements as there is no need to debate reciprocal or "mutual" amounts.[11] Considering the Commission's "longstanding policy to establish standards which will assure competitive equality among wireline and nonwireline carriers,"[12] reciprocal termination is ideal.

---

[11] As explained in Section II.A., it obviates the need for tariff filing requirements.

[12] See Interconnection Declaratory Ruling, 2 FCC Rcd 2919, note 54 (citing Allocation of Frequencies in the 150.8-162 Mc/s Band (Guardband), 12 FCC 2d 841, 849, recon. denied, 14 FCC 2d 269 (1968), aff'd sub nom. Radio Relay Corp. v. FCC, 409 F2d 322 (2d Cir. 1969)).

Reciprocal termination retains its attractiveness as a compensation model regardless of the physical point of CMRS interconnection to the LEC network. Contrary to the Notice's assertions, reciprocal termination sufficiently approximates the costs of termination whether the interconnection is to the LEC tandem or to an individual end office, or, for that matter, to any other efficient interconnection point in the LEC network. Moreover, adoption of reciprocal termination at this juncture does not require current LEC-CMRS interconnections to remain static and unchanging; rather, carriers should be free to mutually negotiate the most efficient point of network interconnection. And to guard against LEC bargaining power, reciprocal termination should be available regardless of the point of interconnection.

Finally, the policy goals underlying the adoption of the Telecommunications Act of 1996, including those supporting the interconnection and unbundled access provisions, reflect in general a preference for a reciprocal termination solution.

A. Reciprocal Termination Will Properly Account for the Disparity in Market Power Between the LECs and Their CMRS Competitors.

The local exchange companies' substantial, persistent market power is a source of unequal bargaining power in interconnection negotiations with the numerous CMRS providers in the LECs' exchange area. As Drs. Mitchell and Brenner explain:

> Because of the unequal bargaining positions of the parties, and because of the incentive of LECs to use pricing of

> interconnection service to extend their market power, this analysis suggests that private, unconstrained negotiations between LECs and CMRS providers are unlikely to yield efficient interconnection compensation arrangements that are in consumers' interests.[13]

This is a classic case of a monopoly firm negotiating with and among competitive firms. Without Commission intervention and oversight, the advantage in bargaining power may result in the extraction of an unreasonable and/or discriminatory interconnection rate, one that aims to secure for the LEC all of the surplus generated by CMRS. By its nature, such a rate will have no basis in cost, and in consequence will impose inefficiencies and barriers to competition in the adjacent wireless market. To overcome this concern, the Commission should adopt a compensation policy which corrects for this inequality in bargaining positions, and which seeks efficiency and long-term, vigorous competition, within both the wireless marketplace and the local exchange. Reciprocal termination is uniquely tailored to accomplish such a result.

As the interconnection compensation price term is one of the more problematic negotiation issues, reciprocal termination will also inhibit the LECs from exercising their substantial, residual market power to the detriment of CMRS and local exchange competition.[14]

---

[13] Economic Issues paper supra at 8.

[14] The Notice reflects concern, on the part of the Commission, that LECs still possess substantial residual market (continued...)

An examination of the interconnection negotiation process between the LECs and the cellular industry reveals controversies that make prudent government intervention at a time when many new CMRS firms are being established and most existing CMRS firms are expanding rapidly. Initially, there were controversies over the type and form of interconnection available to cellular providers.[15] One of the more contentious issues surrounding this process involved pricing.[16] While these controversies were eventually resolved, they remain instructive. Because of the LECs' market position, there was an inequality of bargaining power between cellular providers and the LECs. This disparity in bargaining power continues today between LECs and CMRS providers. In light of this history, and given the continued existence of disparate bargaining power, the Commission should resolve the pricing issue at the outset for the CMRS industry.

---

[14](...continued)
power which they can exercise to the detriment of CMRS competition. Notice at ¶¶ 2, 11-12.

[15] See, e.g., The Need to Promote Competition and Efficient Use of Spectrum for Radio Common Carrier Services, Memorandum Opinion and Order, 59 RR 2d 1275 (1986); Interconnection Declaratory Ruling, supra.

[16] CTIA advocates limited Commission action, i.e., government mandate of the price term for interconnection. Of course, in complex contracts, when the government prescribes only one variable, the other variables can, and to some extent will, be adjusted to compensate. Considering, though, that the price term is the most nettlesome aspect of the interconnection contract, this limited intervention has great utility.

It is important to note at the outset that the controversies surrounding interconnection, especially the price term, are not new; they have repeatedly arisen since the infancy of telecommunications markets. Such disputes are not service specific; instead they affect numerous telecommunications markets, including customer premises equipment ("CPE"), long distance, CAP and international markets.[17] An examination of the various approaches taken demonstrates that key considerations in assessing the optimum arrangement include the relevant costs associated with its adoption and the degree of competitiveness of the relevant networks which will provide mutual message termination settlements.[18] The lessons learned from the resolution of these controversies counsel a solution based upon reciprocal termination.

CPE and Long Distance Models

Both the CPE (zero interconnection fee) and the long distance (access charge) interconnection models are designed to address controversies occurring when one party (e.g., the LEC) has market power, and the other party (the CPE user or the IXC)

---

[17] For a general discussion of these controversies, see Gerald W. Brock, The Telecommunications Industry: The Dynamics of Market Structure (1981); Telecommunication Policy for the Information Age: From Monopoly to Competition (1994).

[18] The Internet "sender keep all" approach provides a current example of a reciprocal termination system being used in a competitive market, i.e., the commercial access companies compete with one another but do not compensate each other with revenues for the termination of traffic.

operates in a more competitive market. The policy concern underlying both models was "to ensure that the competitor could receive access to the monopolized market at an appropriate price."[19]

In Computer Inquiry II, the Commission decided that it would no longer regulate CPE under Title II nor would it allow carriers to continue to include CPE in the rate base.[20] The Commission concluded that interstate service rates were being used to cross-subsidize CPE, thereby thwarting new entry into the CPE market.[21] By removing CPE from the control of the carrier, the Commission correctly anticipated that the equipment market would become competitive.

The Commission's policy not only allowed for interconnection, but also prevented carriers from charging their customers for interconnection of non-carrier CPE (zero cost interconnection). The zero cost interconnection policy eliminated the carriers' ability to impose an interconnection charge as a means of protecting their CPE monopolies (i.e., to impose unreasonable interconnection fees to effectively

---

[19] Gerald W. Brock, Interconnection and Mutual Compensation with Partial Competition, a study prepared for Comcast Corporation, at 17 (Appendix), reprinted in Gerald W. Brock, The Economics of Interconnection, (April 1995).

[20] Final Decision, Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), 77 FCC 2d 384, 388 (1980).

[21] Id. at 441-445.

discourage consumers from switching equipment). The CPE market today is highly competitive. The zero cost interconnection rule appears instrumental in correcting for the competitive imbalance. This lesson has direct application for LEC-CMRS interconnection.

In the IXC market, government policies designed to protect universal service governed the interconnection model finally adopted. When the Modified Final Judgment ("MFJ") required separation of long distance services from local services:

> the CPE [zero cost interconnection] approach to long distance financial arrangements would have eliminated the complex set of payments among telephone companies. It would have caused a substantial increase in local telephone rates as well as possibly threatening the availability of telephone service in high-cost rural areas.[22]

Concluding, as a matter of policy, that a system of subsidies needed to be created to maintain the price of local telephone service throughout the country, the Commission adopted a two-part local exchange subsidy: (1) end users paid a non-traffic sensitive subscriber line charge;[23] and (2) IXCs paid a traffic sensitive "carrier to carrier" access charge for the LEC-provided service of reaching local customers.[24] The direct result of this subsidy was the creation of a system of non-cost-based pricing, i.e., the price for local service is kept

---

[22] Gerald W. Brock, Telecommunications Policy for the Information Age: From Monopoly to Competition at 176 (1994).

[23] While this flat-rate charge had the economic effect of increasing local rates, it appeased state regulators who opposed any increase in local telephone rates. Id. at 187-193.

[24] Id. at 186.

artificially low, while the price for long distance service is kept artificially high. This factor adversely affects competition and efficiency by skewing both consumption and investment. Among other things, it leaves wireless firms at a disadvantage in seeking to compete for local exchange business.

In recognition of these drawbacks, the Commission has expressly committed itself to access charge reform. CTIA supports the Commission's efforts in this regard.

CAP Model

The CAP model, like the IXC model, reflects the Commission's attempt at balancing the realities of competition with the subsidies built into the telephone network.[25] Under this model, though, while the two relevant firms -- the LECs and the CAPs -- are competitors, CAPs are treated for regulatory purposes more as end users than co-carriers with regard to termination charges. This likely results from the fact that, at the outset, LECs

---

[25] In the Expanded Interconnection proceeding the Commission established pricing rules for special access and switched access interconnection. Expanded Interconnection with Local Telephone Company Facilities, Report and Order and Notice of Proposed Rulemaking in CC Docket 91-141, 7 FCC Rcd 7369 (1992) ("Special Access Order"); Second Report and Order and Third Notice of Proposed Rulemaking, 8 FCC Rcd 7374 (1993) ("Switched Access Order"). The rules require LECs to tariff new interconnection pricing arrangements based directly on the cost of the interconnection services plus the addition of uniform overhead loadings. Special Access Order at 7429; Switched Access Order at 7417; see also Special Access Order note 291 (The Commission permitted the LECs to include overhead loading because without it, all other LEC services would be required to recover a greater share of overhead costs or the LECs would lose revenue).

terminated CAP traffic, but there was no reciprocal termination service on the part of the CAPs.

Realizing the harmful competitive impact that a general subsidy, resembling the IXC subsidy, could have if applied to CAPs, the Commission placed the burden upon the LECs to demonstrate the harm directly caused by competitive access prior to imposing any subsidy.[26] This action reflects an understanding that it would be unreasonable to require a CAP to subsidize its competitor unless the LEC was suffering a harm or cost as a result of interconnection. Of course, this action does not address the underlying status -- carrier or customer -- accorded the CAP.

International Settlements Model

The most likely alternative compensation model to reciprocal termination for LEC to CMRS interconnection is the international

---

[26] While the Commission restated its policy that all market participants should contribute to the support flows it has regulated into the LEC rates, it concluded that the only subsidy that could be adversely affected by CAP interconnection is the over-allocation of General Support Facilities ("GSF") costs to special access. Special Access Order at 7437. Rather than mandate a contribution requirement into the special access interconnection rules, the Commission chose to eliminate the GSF support flows entirely. Amendment of Part 69 Allocation of General Support Facility Costs, Report and Order in CC Docket 92-222, 8 FCC Rcd 3697 (1993). The Commission, however, gave the LECs an opportunity to demonstrate that other subsidies, besides GSF, would be adversely affected by CAP interconnection and should therefore be compensated for through a CAP contribution. Special Access Order at 7438; see also 47 C.F.R § 69.122.

settlements model.[27] The marketplace circumstances are very similar -- a monopoly firm on one side of the transaction, competitive firms on the other.

The international experience compels the conclusion that a similar mutual compensation model would be utterly unsatisfactory for LEC to CMRS interconnection. The international settlements model is governed by a system of mutual compensation, i.e., a system whereby each interconnector compensates the other for the termination of traffic based upon a pre-determined uniform charge.[28] While mutual compensation could be efficient in a market where both of the interconnecting firms are monopolists, the international settlements experience demonstrates the many problems in practice; it also demonstrates that its utility is reduced if one side of the market becomes increasingly competitive.[29]

In international settlements, the compensation rate is determined through agreements between the U.S. carrier and the foreign (usually monopoly) postal, telephone and telegraph administration ("PTT"). The policy, dating back to the 1930s, is

---

[27] Under this model, as with the CPE and the IXC model, the relevant firms are not competitors, but instead cooperate to provide one service. The relevant firms, though, are considered co-carriers (unlike the CAPs), analogous to the LEC to CMRS model.

[28] At times, the government pre-determines the charge.

[29] See Policy Statement of International Accounting Rate Reform, FCC 96-37 (rel. Jan. 31, 1996).

based on the assumption that the domestic and foreign carrier each possesses market power and therefore will be able to negotiate an equitable arrangement. Under this model, though, a monopolist PTT will have an advantage if it is negotiating with a carrier in a competitive market because it can require the competing carriers to bid against one another, a practice known as whipsawing.

As competition has developed in the U.S. market for the provision of international services, the Commission created the "uniform settlements policy" to protect domestic carriers from whipsawing.[30] This policy is designed to prevent foreign PTTs from discriminating among U.S. carriers by requiring that the operating agreements of all U.S. carriers providing similar service to the same destination contain identical accounting rates, settlement rates, and division of tolls.[31]

While competition in the U.S. market results in lower domestic prices for international telephone calls, as a direct result of mutual compensation principles, domestic carriers pay billions of dollars annually to foreign PTTs. "Between 1985 and 1994, U.S. carriers paid $26 billion in settlement payments to

---

[30] See, e.g., Mackay Radio and Telegraph Co., 25 FCC 690 (1951), rev'd on other grounds sub nom. RCA Communications, Inc. v. FCC 201 F.2d 694 (1953); TRT Telecommunications Corp., 46 FCC 2d 1042 (1984).

[31] See Implementation and Scope of the International Settlements Policy for Parallel International Communications Routes, Order on Reconsideration in CC Docket 85-204, 2 FCC Rcd 1118 (1987); Further Reconsideration, 3 FCC Rcd 1614 (1988).

foreign carriers; as much as one half of these payments may have exceeded the actual costs of terminating calls."[32] Essentially, the foreign PTT is able to continue charging monopoly prices, thereby limiting the number of calls terminated in the U.S., while the U.S. carrier is often charging its customers near cost, directly increasing the number of outgoing calls.[33] This increases the foreign PTT's revenues because it will terminate a greater number of calls. In effect, U.S. consumers pay billions of dollars annually to subsidize foreign telephone and postal rates.[34]

As demonstrated by the international settlements experience, a mutual compensation scheme can produce severely adverse consequences in markets where only one provider possesses market power.[35] It requires significant (and costly) government regulation, including rate regulation, and record-keeping requirements for the participating firms. Moreover, as discussed

---

[32] Policy Statement on International Accounting Rate Reform, at 6 (footnote omitted).

[33] Leland L. Johnson, International Telecommunications Regulation, New Directions in Telecommunications Policy 92, 99 (1989) ("competing carriers may be willing to lower their collection rates in order to get favorable operating agreements for return traffic. The PTTs unambiguously gain if U.S. Collection rates fall (with constant accounting rates) since the volume of the PTT's terminating traffic, and their revenues, from the United States would rise.").

[34] Id. at 101.

[35] Its utility in a market where the relevant firms are competitors is questionable as well.

below, tariff filing requirements, even if imposed upon the LEC, simply have no place in a burgeoning market such as CMRS. Considering its limited efficacy in competitively-developing markets, the utility of mutual compensation for LEC to CMRS interconnection compensation is questionable.[36]

Experience thus shows that reciprocal termination is the most useful model for LEC to CMRS interconnection compensation. There exist different levels of market power among the market participants (i.e., the LEC and the CMRS provider). In addition, the two firms are competitive, i.e., there exists both the incentive as well as the ability on the part of the LEC to exercise its bargaining power to extract an unreasonable and/or discriminatory interconnection compensation rate. Reciprocal termination helps guard against such a result.

B. Reciprocal Termination Sufficiently Approximates Carrier Marginal Costs for Traffic Termination.

A workable interconnection compensation arrangement must meet two primary economic requirements: First, an interconnection compensation arrangement must allow carriers to recover efficiently their cost of terminating traffic. Second, an interconnection compensation arrangement should maximize the

[36] Reciprocal termination can be thought of as another form of mutual compensation, where the compensation rate is set at $0.00.

net economic efficiency of pricing signals.[37] As demonstrated below, no interconnection compensation alternative perfectly fulfills either of these requirements. However, on balance, reciprocal termination fulfills these requirements to a greater extent than any other available (and implementable) alternative.[38]

1. Reciprocal Termination Will Allow Carriers to Recover the Cost of Terminating Traffic.

Although under reciprocal termination neither carrier receives revenue for terminating traffic originating on other networks, it does not necessarily follow that reciprocal termination will inhibit carriers' ability to recover termination costs. First, it is important to remember that reciprocal termination involves a mutual obligation to terminate traffic. The cost of this obligation is the cost of providing termination services; the cost of providing termination becomes part of the cost of doing business for each carrier. Thus, if total termination costs are approximately equal, neither carrier bears a disproportionate burden. Reciprocal termination can result in each carrier bearing essentially the same total cost to terminate

---

[37] Efficiency gains associated with an interconnection arrangement must be netted against the cost of obtaining those gains. These costs include the cost of implementing and maintaining the interconnection arrangement, as well as dynamic costs associated with the interconnection arrangement's effect on competition and competitive entry.

[38] The economic assessment of reciprocal termination and alternative interconnection arrangements outlined below is based upon the Economic Issues paper.